

Message Text

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SUBJ: GOA SEEKS TO EXPAND EUROPEAN RECOVERY PROGRAM (ERP) FUNDS
FOR ECONOMIC STIMULATION

REF: VIENNA A-62

1. SUMMARY: AS ONE ELEMENT IN ITS 1976 ECONOMIC STIMULATION PROGRAM, THE GOA FINANCE MINISTER HAS BEEN AUTHORIZED TO GRANT THE ERP FUND ONE-TIME AUTHORITY TO EXPAND ITS LENDING RESOURCES BY ISSUING ITS OWN LONG-TERM, LOW-INTEREST OBLIGATIONS IN THE AMOUNT OF AS 1.5 BILLION (\$81.3 MILLION CONVERTED AT AS 18.45 EQUALS \$1.00). AUSTRIAN COMMERCIAL BANKS, WHICH PRESENTLY FIND THEMSELVES WITH CONSIDERABLE EXCESS LIQUIDITY AND LOW CREDIT DEMAND, ARE THE INTENDED PURCHASERS OF THIS OPEN MARKET PAPER. THE BANKS, IN TURN, WILL BE ABLE TO HAVE THE ERP FUND DEBENTURES REDISCOUNTED AT THE AUSTRIAN NATIONAL BANK (ANB) AT SUCH TIME AS BANK LIQUIDITY TIGHTENS. THE PROPOSAL HAD BECOME SOMETHING OF A DOMESTIC POLITICAL ISSUE WITH SOME CONSERVATIVE ELEMENTS CRITICIZING IT AS BEING POTENTIALLY INFLATIONARY AND IN CONFLICT WITH AUSTRIAN LEGISLATION. EMB OFFICERS HAVE DISCUSSED PLAN WITH AUSTRIAN LEGISLATION. EMBA OFFICERS HAVE DISCUSSED PLAN WITH SEVERAL GOA

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OFFICIALS, (INCLUDING ANB DIRECTOR GENERAL HEINZ KIENZL), WHO

STRONGLY DEFENDED IT, AND EXPRESSED VIEW THAT IT WAS CONSISTENT WITH THE 1961 ERP COUNTERPART SETTLEMENT AGREEMENT BETWEEN U.S. AND AUSTRIA AND NOT CONTRARY TO DOMESTIC ERP LAW. HOWEVER, SINCE GOA PLAN INVOLVES THE ERP FUND IN ACTIVITIES NOT CONTEMPLATED IN 1961, THE EMBASSY REQUESTS THAT THE DEPT REVIEW IT AND PROVIDE US WITH A JUDGMENT ON LEGALITY AND CONSISTENCY OF THE PROPOSAL WITH THE ERP AGREEMENT. END SUMMARY.

2. GOA PLAN--

AS PART OF ITS 1976 ECONOMIC STIMULATION PLAN, GOA ANNOUNCED ITS INTENTION LATE IN JANUARY TO EXPAND THE AMOUNT OF LOW-INTEREST, LONG-TERM FUNDS WHICH COULD BE LENT FOR DOMESTIC INVESTMENT PROJECTS BY THE ERP FUND AND THE OESTERREICHISCHE INVESTITIONSKREDIT-AG (AUSTRIAN INVESTMENT CREDIT CORP--AICC). ON MARCH 2, CABINET APPROVED A PLAN THE MAJOR PROVISIONS OF WHICH (WITH PARTICULAR EMPHASIS ON INVOLVEMENT OF ERP FUND) ARE AS FOLLOWS:

- THE ERP FUND AND THE AICC ARE TO BE AUTHORIZED BY FINANCE MINISTER TO ISSUE THEIR OWN DEBENTURES IN AMOUNTS OF AS 1.5 BILLION (\$81.3 MILLION) AND AS 500 MILLION (\$26.9 MILLION), RESPECTIVELY;
- A PREREQUISITE FOR GRANTING OF ISSUING AUTHORITY IS A WRITTEN COMMITMENT BY ERP FUND TO ANB THAT (A) ALL PROCEEDS DERIVED FROM AMORTIZATION OF INVESTMENT CREDITS EXTENDED FROM THE NEW RESOURCES; (B) REALIZATIONS FROM SALE OF COLLATERAL POSTED BY BORROWERS, AND (C) ACCRUALS TO THE NEW SEPARATE RESERVE FUND (DISCUSSED BELOW) SHALL BE USED EXCLUSIVELY FOR REDEMPTION OF ERP FUND DEBENTURES.
- THE ERP FUND NOTES ARE EXPECTED TO BE DUE IN 10 YEARS AND CARRY AN INTEREST RATE OF ABOUT 4-1/8PERCENT
- COMMERCIAL BANKS, WHICH CURRENTLY HAVE LARGE, NON-INTEREST EARNING, EXCESS RESERVES WITH ANB AND WHICH ARE FACED WITH SLUGGISH LOAN DEMAND, WILL PURCHASE ERP FUND AND AICC OBLIGATIONS.
- AT SUCH TIME AS BANK LIQUIDITY TIGHTENS, COMMERCIAL BANKS WILL BE ABLE TO REDISCOUNT THE NOTES AT ANB;
- THE ANB RESERVES RIGHT, HOWEVER, TO NEUTRALIZE THE EXPANSIVE EFFECTS OF SUCH OPEN MARKET OPERATIONS BY CONTRACTIVE ACTION, E.G. BY INCREASING MINIMUM RESERVE REQUIREMENTS;
- THE INCREASED ERP FUND AND AICC RESOURCES WILL BE LENT AT LIMITED OFFICIAL USE

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A 5 PERCENT INTEREST RATE AND MIXED WITH COMMERCIAL BANK FUNDS TO PRODUCE BLENDED CREDITS AT LESS THAN MARKET RATES. THE 5PERCENT INTEREST RATE TO BE CHARGED ON THE ERP FUND PORTION OF THESE LOANS IS TO BE BROKEN DOWN IN FOLLOWING MANNER:

- 4-1/8PERCENT FOR SERVICING ERP FUND NOTES;
- 3/8PERCENT AS A SERVICE CHARGE TO THE BANKS; AND
- 4/8PERCENT FOR CREATION OF A SPECIAL RESERVE, SEPARATE FROM BUT ADMINISTERED BY, ERP FUND FOR POSSIBLE BAD LOANS.

3. GOA MOTIVATION--

IN LIGHT OF CONTINUED SLACK IN DOMESTIC EXPENDITURES ON PLANT AND EQUIPMENT GOA IS ANXIOUS TO MAKE INVESTMENT CREDITS AVAILABLE ON AS ATTRACTIVE TERMS AS POSSIBLE. AT SAME TIME, FOR POLITICAL AND ECONOMIC REASONS, GOA DOES NOT WITH TO ADD TO ALREADY LARGE PORJECTED 1976 FEDERAL DEFICIT BY DIRECT INTEREST SUBSIDIZATION THROUGH THE BUDGET. ANB DIRECTOR GEN KIENZL, WITH WHOM EMBOFFS HAVE DISCUSSED THE PLAN, GAVE TWO REASONS FOR PLAN IN ADDITION TO THE DESIRE TO PLACE DOWNWARD PRESSURE ON CREDIT COSTS;

--GOA WISHES TO OFFSET THE EROSION THROUGH INFLATION OF THE ERP FUND'S REAL LENDING RESOURCES IN ORDER TO PRESERVE IT AS AN EFFECTIVE POLICY INSTRUMENT; AND

--IN VIEW OF DISPROPORTIONATELY LARGE AUSTRIAN BORROWINGS ABROAD OVER PAST TWO YEARS, AUSTRIAN MONETARY AUTHORITIES WANT TO TRY TO MOBILIZE DOMESTIC CREDIT RESOURCES MORE EFFECTIVELY.

4. LOCAL REACTION--

THE GOA PLAN HAS BECOME SOMETHING OF A POLITICAL ISSUE. CONSERVATIVE OPPOSITION FINANCIAL EXPERTS, INCLUDING FORMER ANB PRESIDENT WOLFGANG SCHMITZ HAVE ATTACKED IT AS BEING POTENTIALLY INFLATIONARY AND CONTRARY TO ANB AND ERP FUND LEGISLATION. WHILE ADMITTING THE IDEA IS A NEW ONE, THE GOVERNING SOCIALISTS MAINTAIN THAT IT IS ENTIRELY LEGAL.

5. RELATIONSHIP TO ERP SETTLEMENT AGREEMENT--

IN DISCUSSING THE MATTER WITH EMBOFFS, GOA OFFICIALS EXPRESSE THE VIEW THAT IT WAS FULLY CONSISTENT WITH THE 1961 ERP COUNTERPART SETTLEMENT AGREEMENT. WOLFDIETRICH GRAU, SPECIAL ASSISTANT TO STATE SECRETARY VESELSKY IN CHANCELLOR'S OFFICE, DESCRIBED IT AS IN ESSENCE AS MEANS BY WHICH THE ERP FUND LIMITED OFFICIAL USE

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ADMINISTERS A CONCESSIONAL LENDING PROGRAM SIMILAR TO, BUT DISTINCT FROM, ITS OWN. HE SAID THAT THE CREATION OF A SEPARATE RESERVE FUND IS BEING DONE PRECISELY TO AVOID HAVING THE ERP FUND ITSELF ASSUME THE RISK FOR THE NEW LOANS.

6. COMMENT: THE GOA PLAN WOULD INVOLVE THE ERP FUND IN ACTIVITIES NOT CONTEMPLATED AT THE TIME OF THE 1961 COUNTERPART SETTLEMENT AGREEMENT AND POSSIBLY NOT IN ACCORD WITH ARTICLE II OF THE SAME AGREEMENT. AT THE SAME TIME, THE PROPOSAL DOES NOT APPEAR TO BE EXPRESSLY PROHIBITED BY THE AGREEMENT, AS WAS THE CASE IN LAST YEAR'S ABONDONED SCHEME TO USE GRANTS FROM ERP FUND RESOURCES TO SUBSIDIZE INTEREST RATES ON DOMESTIC CREDITS. THE EMBASSY REQUESTS THAT THE DEPT REVIEW THE GOA PLAN AND PROVIDE US WITH JUDGEMENT OF LEGALITY AND CONSISTENCY OF THE PROPOSAL WITH THE 1961 ACCORD.BUCHANAN

NOTE BY OC/T: REFERENCE NOT AVAILABLE.

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